

*United States Court of Appeals
for the Second Circuit*



APPELLEE'S BRIEF

ORIGINAL
WITH PROOF
OF SERVICE

75-6001

UNITED STATES COURT OF APPEALS

for the

SECOND CIRCUIT

PPG INDUSTRIES, INC.,

B
PK
Plaintiff-Appellee,

-against-

THE HARTFORD FIRE INSURANCE COMPANY,
NEW YORK STATE TAX COMMISSION, STATE
OF NEW YORK, CAR COLOR, INC. and HENKIN
& HENKIN, ESQS.,

Defendants,

-and-

UNITED STATES OF AMERICA,

Defendant-Appellant.

ON APPEAL FROM AN OPINION AND ORDER
OF THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK



BRIEF OF PLAINTIFF-APPELLEE

JACOB F. GOTTESMAN
Attorney for Plaintiff-Appellee
420 Lexington Avenue, New York, New York 10017

(4803)

COUNSEL PRESS, INC., 55 West 42nd Street, New York, N.Y. 10036 • PE 6-8460

I N D E X

	<u>Page</u>
Preliminary Statement	1
Issues Presented	1
Statement of the Case	2
A. Proceedings Below	2
B. Facts	3
C. The Basis of the Decision by the Court Below	6
Summary of Argument	7
Argument	8
Point I - The Intent and Purpose of the Security Agreement Was to Guarantee PPG a Legal Right to the Proceeds of the Insurance Policy.	8
Point II - The Reasoning Behind the Opin- ions of the Several Courts Referred to Herein Leads But to One Conclusion-- that PPG Should Prevail.	10
Conclusion	11

TABLE OF AUTHORITIES

	<u>Page</u>
<u>Case:</u>	
Firemen's Fund Insurance Co. v. Ken-Lori Knits Inc., ___ F.Supp. __ (73 C 1242), decided May 8, 1975	6
<u>Statutes:</u>	
Internal Revenue Code:	
Section 6323(a)	7, 8
Section 6323(h)	9
Uniform Commercial Code:	
Section 9-306(1)	8
Section 9-306(2)	8
<u>Other Authorities:</u>	
Coogan, Hogan & Vagts, Secured Transactions under UCC Sec. 12.08(2) at 1276 (Bender's Uniform Commercial Code Service 1973)	9

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

- - - - - X

PPG INDUSTRIES, INC.,

Plaintiff-Appellee,

-against-

THE HARTFORD FIRE INSURANCE COMPANY, NEW YORK
STATE TAX COMMISSION, STATE OF NEW YORK, CAR
COLOR, INC. and HENKIN & HENKIN, ESQS.,

Defendants,

Docket
75-6001

-and-

UNITED STATES OF AMERICA,

Defendant-Appellant.

- - - - - X

BRIEF OF PLAINTIFF-APPELLEE

PRELIMINARY STATEMENT

Defendant-appellant, The United States of America, appeals to this Court from an opinion and order, filed November 11, 1974, which granted the plaintiff-appellee, PPG INDUSTRIES, INC., a priority in a fund belonging to the defendant, CAR COLOR INC., superior to the Government's tax liens. The Opinion and Order is reproduced in the Joint Appendix (JA) at 101-118 and is reported at 384 F. Supp. 91 (S.D.N.Y. 1974) (Connor, J.).

ISSUES PRESENTED

1. Does a valid security interest have a priority over a

tax lien filed subsequent to giving and filing of the security interest.

2. Did the Magistrate err in his conclusion that PPG, the secured party, had a legal right to the proceeds of the insurance policy arising out of the collateral security for the indebtedness.

3. Did Judge Connor err in his view that PPG had a security interest in the insurance proceeds since the parties intended that the insurance proceeds on that collateral be further security for the loan.

STATEMENT OF THE CASE

A. PROCEEDINGS BELOW:

PPG commenced this action on June 26, 1973 in the Supreme Court of New York County to recover a \$7,354.29 cash fund held by the defendant HARTFORD FIRE INSURANCE COMPANY (HARTFORD) which fund was otherwise payable to CAR COLOR. PPG and the other parties to this action, the Government, the New York State Tax Commission, and Henkin & Henkin, Esqs., had claims against CAR COLOR in excess of the fund. The action was removed to the United States District Court for the Southern District of New York. The object of the action was to determine the priority of claims to the fund. The claim of the Government was for taxes due and owing from CAR COLOR.

On July 25, 1974, the Honorable HAROLD J. RABY, United States Magistrate for the Southern District of New York, issued a report (JA at 78-98) in which he fixed the order of priority as follows: Henkin & Henkin, Esqs. received \$2,654.25 for services rendered to CAR COLOR in creating the fund. HARTFORD received \$500.00 for legal expenses incurred as a stakeholder. PPG received \$4,200.04, the balance of the fund. Over the objection of the GOVERNMENT, the order of priority was confirmed on other grounds by the District Court. The GOVERNMENT appeals from that portion of the District Court's Order which granted a priority to PPG superior to the GOVERNMENT'S tax liens.

B. FACTS:

This action was decided by summary judgment upon jointly stipulated facts.

CAR COLOR operated a retail and wholesale paint store in Yonkers, New York. (JA at 129). CAR COLOR purchased a paint inventory from PPG. On September 28, 1970, CAR COLOR and PPG entered into a security agreement. A financial statement reflecting the security agreement was filed with the Westchester County Clerk on October 8, 1970. The financing statement covered CAR COLOR'S inventory of PPG products as well as the proceeds of the inventory (JA at 63). In addition the security agreement included

"(b) 'Equipment' means those goods, merchandise and other personal property used in Borrower's business." The security agreement defines collateral, "(e) 'Collateral' means the inventory and equipment described herein in which secured party is granted a security interest."

The GOVERNMENT in its brief erroneously limits the security interest of PPG to its inventory, page "3-5" and page "18". Neither the Magistrate nor Judge Connor were ever in doubt as to the extent of the security interest PPG had in the property of the debtor. The two courts accepted the document without reservations or qualifications as to the extent of PPG's interest therein. At this stage we point out that PPG had filed the entire agreement with the Secretary of State and the County Clerk. Generally, the abbreviated financing statement is filed which could lead to an error such as the GOVERNMENT is laboring under. In addition the security agreement included, "5. Borrower (CAR COLOR) will . . . (f) keep the Inventory and Equipment insured for the benefit of Secured Party (PPG) (to whom loss shall be payable) and in such amount and with such companies and against such risks as may be satisfactory to Secured Party; pay the cost of all such insurance; and deliver certificates evidencing such insurance to Secured Party; and Borrower assigns to Secured Party all right to receive

proceeds of such insurance, directs any insurer to pay all proceeds directly to Secured Party, and authorizes Secured Party to endorse any draft for such proceeds . . ." (JA at 61).

On December 10, 1970 CAR COLOR obtained a fire insurance policy in the amount of \$25,000 from HARTFORD (JA at 25, 57). The only named insured or loss-payee on the policy was CAR COLOR (JA at 57). This insurance policy was not obtained by CAR COLOR in compliance with section 5 (f) of the security agreement because PPG was not named the loss-payee nor was HARTFORD instructed to delivery any insurance proceeds to PPG. CAR COLOR's Premises was substantially destroyed by a fire on December 23, 1971 (JA at 57). Under the terms of the security agreement PPG was invested with a broad power of attorney not only to claim the policy, to receive the proceeds, but also to endorse any draft for such proceeds on the day of the fire, assuming the proceeds were available and the draft made on that date. The debtor in assigning its interest to PPG to receive the proceeds of such insurance gave PPG an irrevocable interest therein which could not be interfered with by the debtor or anyone standing in relationship to the debtor or claiming under.

HARTFORD disclaimed liability under the policy claiming that the fire was caused by arson attributable to CAR COLOR (JA at 135).

On November 29, 1972, CAR COLOR commenced an action in the Supreme Court of New York County against HARTFORD demanding judgment in the amount of \$22,549.75 for failure to make payment to CAR COLOR under the insurance contract. That action was removed to the United States District Court for the Southern District of New York. The District Court found that HARTFORD had not established its defense of arson. On April 25, 1973, the Court entered a judgment in favor of CAR COLOR and against HARTFORD in the amount of \$7,354.29 plus interest retroactive to April 3, 1972 (JA at 57). The judgment covered all the losses sustained by CAR COLOR which stemmed from the destruction of the secured property pledged to PPG.

C. THE BASIS OF THE DECISION BY THE COURT BELOW:

Magistrate Raby and Judge Connor reached the same result. Each concluded that the interest of PPG in the fund could not be contravened by the GOVERNMENT's tax lien regardless of the points of time. The rationale of their opinions was to the effect that the intent of the parties governed and that PPG unmistakably was entitled to the fire proceeds once the fire occurred.

Chief Judge Mishler sitting in the Eastern District in Firemen's Fund American Insurance Co., vs. Ken-Lori Knits Inc. (73 C 1242) decided on May 8, 1975 in similar fashion decided on practically identical facts that the cumulative effect of the

security agreement and the language thereof made clear the intention of the parties to give the proceeds of the fire insurance to the secured party. Judge Mishler found that, he aligns himself with Magistrate Raby, in that he said that "Ambassador's lien became choate at the date of the fire, October 15, 1972, when Firemen's obligation to pay on the policy accrued. It may well have become choate when, with the perfecting of the security agreement, Ambassador obtained present rights in the insurance policy to receive payments in the future in the event of damage to the property. * * * * * * * * * He went on to say, "Under the UCC and the plain provisions of the insurance policy, Ambassador has priority in its claim on the insurance proceeds over the Government whose tax lien is subsequent in time."

Judge Connor said in his concluding paragraph:

"It is beyond doubt that PPG had a security interest in Car Color's inventory and that the parties intended the proceeds of the insurance on that collateral to be further security for the loan. Thus, in view of the policy considerations behind Article 9, as well as the policy of 26 U.S.C. Sec. 6323 to give preference to security interests as defined by that provision, we are impelled to the conclusion that PPG had a security interest in the proceeds of the insurance which takes precedent over the government's lien."

SUMMARY OF ARGUMENT

The Several findings by the members of the Court below in favor

of PPG should not be disturbed.

ARGUMENT

POINT I

THE INTENT AND PURPOSE OF THE SECURITY AGREEMENT
WAS TO GUARANTEE PPG A LEGAL RIGHT TO THE
PROCEEDS OF THE INSURANCE POLICY.

It has been contended throughout by PPG that it intended that its debt be completely secured by the inventory, and equipment, and that it accomplished this by the filing of the security agreement. It has likewise claimed that the only way to respect the intent of the parties to the agreement is to allow it to reach the insurance proceeds.

The GOVERNMENT does not contest that PPG's security interest, under New York law, was perfected before the tax liens were filed.

Under Section 9-306 (2) of the UCC:

"a security interest continues in collateral notwithstanding sale, exchange or other disposition thereof by the debtor . . . and also continues in any identifiable proceeds including collections received by the debtor."

Under Section 9-306 (1) of the UCC:

"'Proceeds' includes whatever is received when collateral or proceeds is sold, exchanged, collected or otherwise disposed of."

Section 6323 (a) of the Internal Revenue Code provides that

"The lien imposed by section 6321 shall not be valid as against any purchaser, holder of a security interest, mechanic's lienor, or judgment lien creditor until notice thereof . . has been filed . . ."

The lien of the GOVERNMENT sprang into existence on May

4, 1972. The fire occurred on December 23, 1971 at which time PPG's right became choate.

PPG qualified as a holder of a security interest within the definition of Section 6323 (h) of the Internal Revenue Code which provides that:

"The term 'security interest' means any interest in property acquired by contract for the purpose of securing payment or performance of an obligation or indemnifying against loss or liability. A security interest exists at any time (A) if, at such time, the property is in existence and the interest has become protected under local law against a subsequent judgment lien arising out of an unsecured obligation, and (B) to the extent that, at such time, the holder has parted with money or money's worth."

By the time the GOVERNMENT filed its lien in May of 1972 it is clear that PPG's interest in the inventory and equipment was choate and was known to the GOVERNMENT for the identity of the lienor, and the property subject to the lien were known by October, 1970; and, by April, 1972 there was a judgment in favor of PPG against CAR COLOR for \$12,300.90.

See Coogan, Hogan & Vagts, Secured Transactions under the U.C.C. Sec. 12.08 (2) at 1276 (Bender's Uniform Commerical Code Service 1973).

Thus, PPG's lien is entitled to the priority accorded it by the Magistrate.

POINT II

THE REASONING BEHIND THE OPINIONS OF THE SEVERAL COURTS REFERRED TO HEREIN LEADS BUT TO ONE CONCLUSION--THAT PPG SHOULD PREVAIL.

PPG is entitled to the priority accorded it by the several Judges below as its security interest in the insured properties was transferred to the insurance proceeds when the property was destroyed by fire. On that date PPG contractually, the possessor of the assignment invested with the Power of Attorney to endorse, could claim the fire loss. The fire loss damage claim was the tangible successor to the property, it was clear, visible and subject to the immediate possessory claim of PPG. The real intentment of the agreement was to so secure PPG against loss or liability.

The hornbook rule of law is still extant, namely, that the contractual intent shall be drawn from the lines of the agreement. The giving of the right to endorse the check to PPG was the icing on the pastry. CAR COLOR obligated itself to obtain insurance for its own benefit but, to secure PPG in furtherance thereof. The intentment of the agreement was simply to protect PPG against dissipation of the collateral by sale or other disposition or from the possibility of destruction. In fact it cannot be denied, but for the insistence on the part of PPG that the debtor shall obtain fire insurance there would be no funds to fight for.

We accept and adopt and ask this Court to see eye to eye



with Judge Connor, Chief Judge Mishler and the Magistrate. They all expounded their theories and their conclusions in the opinions they rendered all of which necessarily terminate in favor of PPG.

By legal definition and statute the GOVERNMENT could levy only on that property which the debtor owned and possessed when the assessment was filed in May of 1972. There was nothing visible on that date on which the lien could attach. The property and its replacement, the damage claim, were the property of PPG to whom it had been assigned by a proper instrument containing indelible terms of ownership by PPG. There was nothing in existence on the date of the GOVERNMENT filing on which the lien could latch onto.

CONCLUSION

The judgment of the District Court should be affirmed.

Respectfully submitted,

JACOB F. GOTTESMAN
Attorney for PPG INDUSTRIES, INC.
Plaintiff-Appellee

Received 2 copies of the within
Brief of Plaintiff Appellee
this 17th day of June, 1975.
Signed Barrie P. Iron -
For: Paul J. Curran Esq(s).
Attⁿ to for Defendant Appellant

